

***United States Court of Appeals
for the Second Circuit***



APPELLEE'S BRIEF

To be Argued by

NORMAN S. OSTROW

77-1342

UNITED STATES COURT OF APPEALS

FOR THE SECOND CIRCUIT

Docket No. 77-1342

UNITED STATES OF AMERICA,

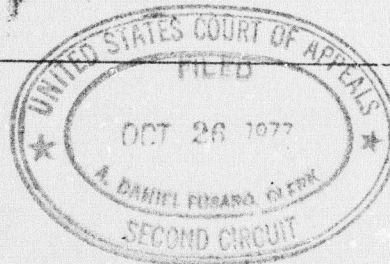
Appellant,

v.

DOUGLAS P. FIELDS, FREDERICK M. FRIEDMAN, PETER S.
DAVIS, ALAN E. SANDBERG, and ERIC BERGE,

Defendants-Appellees.

BRIEF FOR DEFENDANT-APPELLEE ALAN E. SANDBERG



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BRIEF FOR DEFENDANT-APPELLEE ALAN E. SANDBERG

Statement of the Case

This is an appeal by the Government from
an order of the United States District Court for the
Southern District of New York (Haight, J.) dismissing
all of the charges in an indictment against Alan E.
Sandberg* and most of the charges against the other
appellees herein (76 Cr. 1022 (CSH)). The District

*Sandberg, who was originally charged only with mail and
wire fraud concerning receipt of a single finder's fee,
was severed from the main part of the case upon consent
of the Government.

Court struck from the indictment all reference to transactions which were disclosed to the Securities and Exchange Commission ("SEC") by appellees' counsel during negotiation of an SEC civil consent judgment on the ground that certain representatives of the SEC had acted improperly. The Court found the SEC had misled counsel concerning whether a criminal reference would be made and failed to disclose to counsel that the staff of the SEC had already referred the case to the United States Attorney for criminal prosecution. The District Court held, given the circumstances of this case, and "viewed in the context of all that had gone before ..." that the SEC representatives should in fairness have advised counsel and their clients prior to the execution of the consent decrees that the matter had already been referred to the United States Attorney for criminal prosecution. The District Court invoked its inherent supervisory power over the administration of criminal justice and dismissed the indictment which resulted from the SEC's criminal reference.

While appellee Sandberg obviously agrees with the District Court's findings and conclusions,* it is

*Sandberg respectfully joins in each of the briefs and arguments of the other appellees insofar as they are applicable to him, and will not separately reargue the findings and conclusions below.

respectfully submitted that the same conclusion is sustainable on alternate grounds. Our argument is prompted, in part, by a theory advanced by the Government to the effect that the SEC and the United States Attorney's office are wholly distinct Government agencies performing different functions, and therefore the Government cannot be held accountable for the misconduct of SEC employees. The Government's theory, which we reject in this case, may have been conceived by the fact that the SEC's legal authority to make a criminal reference to the Justice Department is strictly circumscribed by statute and regulation. Those statutes and regulations clearly provide that only the Commission itself has the authority to make a criminal reference, and further that authority has not been delegated to SEC employees. In the present case, those statutes and administrative regulations were arbitrarily ignored in that the Commission itself did not make the decision as to whether a reference should be made; indeed, neither the Commission nor other high level SEC officials who are required by regulation to review a proposed reference were even consulted. Accordingly,

the informal criminal reference employed here was an invalid and void Governmental action. Since the indictment was the immediate and direct consequence of that illegal action, it must be dismissed.

The Government's response to Sandberg's first argument invites his second. The Government not only defends the SEC's disregard of its rules and regulations regarding a criminal reference, it has become a willing participant in that extra-legal informal criminal reference system. In view of this close relationship, the United States Attorney cannot now claim to be immunized from the consequences of the misconduct of the SEC employees who were acting within the purview of a procedure which the SEC and the United States Attorney's office have contrived for their mutual benefit. The conduct criticized below was designed to extract a civil settlement, including disgorgement

of a substantial sum, as well as to bring about a criminal prosecution for those same acts. In short, the SEC personnel were in fact "arms of the prosecutor" when they acted in the improper manner found by the Court below. Therefore, the Government prosecutors are accountable for their actions.*

*Certain limited observations peculiar to Sandberg's position are appropriate here to augment those arguments advanced by other counsel for the other appellees. First, he cannot be made whole by the remedy proposed by the Government, which is to set aside "the defendants obligations further to perform pursuant to the terms of the civil settlement" (Gov't. Br. 4). Sandberg has fully performed his obligations under that consent decree by transferring to TDA for cancellation 35,000 shares of TDA stock. Secondly, the Government's "unclean hands" argument cannot apply to Sandberg as he was not indicted for those actions (Gov't. Br. 32-33).

QUESTIONS PRESENTED

1. Does the SEC's violation of the statutes, rules and regulations concerning the making of a criminal reference require dismissal of the resulting indictment?

2. Is the United States Attorney accountable for the misconduct of SEC employees where the United States Attorney participates in and benefits from an illegal criminal reference?

Statement of Facts

A. The "Criminal Reference"

The circumstances surrounding the criminal reference in this case are not in dispute. The Government stipulated below that on December 1, 1975 Jeffrey Tucker, at that time a Branch Chief in the New York office of the SEC, "referred" the TDA matter to John Wing, Assistant United States Attorney for the Southern District of New York and Assistant in Charge of the Fraud Unit by telling him orally of the matter and on the same day sending him copies of the pleadings in Securities and Exchange Commission v. TDA Industries, et al. (App. 297-99, 205, 639).*

There is no question that the SEC initiated the contact with the United States Attorney's office.** As early as October 1975, Stuart Perlmutter, SEC staff attorney, advised Ira Sorkin, another Assistant United States Attorney, about making a criminal case

*The Appendix is referred to hereinafter as "App.". The Transcript of the hearing below is referred to hereinafter as "Tr.". The Government's Brief on Appeal is referred to hereinafter as "Gov't. Br.").

**There is testimony below as to the propriety of the SEC responding to an inquiry from the United States Attorney's office with regard to matters under investigation by the SEC (App. 548-49). That did not happen here; the SEC volunteered the information to the United States Attorney's office.

in the TDA matter (App. 644-46). As is set forth in detail in the briefs of the other appellees, neither Perlmutter nor Tucker, nor Sorkin for that matter, ever advised appellees or their counsel of the referral to the United States Attorney (App. 617, 647-48). More significant to Sandberg's first argument is the fact that neither the Commission, the SEC General Counsel, the Director of the Division of Enforcement (Stanley Sporkin), the Office of Criminal Reference and Special Proceedings, the Regional Administrator (William Moran) nor his assistant (Donald*Malawsky),* nor anyone at that high level within the SEC was informed or consulted with respect to either criminal reference (App. 614, 624). Indeed, it was not until April 25, 1977 that the Commission retroactively, and "without recommendation", approved the reference (App. 295-96).

B. The Decision Below

The Court below found that by making an informal criminal reference, the SEC lawyers "followed a practice which had grown up over the past several years" which in fact "accounts for the majority of present-day criminal references" (App. 56-57). The

*There was a conflict in testimony as to Mr. Malawsky's participation in the reference (App. 624), but he denies knowledge of it (App. 651-53).

Court refused to invalidate the informal criminal reference procedure, stating (App. 69):

"Nothing in the statute or regulations expressly prohibits any method of criminal reference other than a reference by the Commissioners themselves; accordingly prohibition must be found, if at all, by necessary implication. But I conclude that the SEC may, without violating its governing statutes or its own regulations and procedures, sanction this method of informal criminal references."

Argument

POINT I

THE INDICTMENT SHOULD BE DISMISSED
BECAUSE THE GOVERNMENT DISREGARDED
THE STATUTES, RULES AND REGULATIONS
CONCERNING A CRIMINAL REFERENCE

Appellee Sandberg maintains that this indictment should be dismissed on the ground that it was the direct and immediate consequence of an informal criminal reference which was absolutely void. We respectfully suggest the only way to remedy the SEC's utter disregard of its own rules and regulations concerning a criminal reference is to undo the result of that reference -- the indictment.

A. The Applicable Statutes, Rules
And Regulations Do Not Permit
An Informal Criminal Reference

Appellees do not question the SEC's statutory authority to refer matters to the Justice Department for criminal prosecution. The Securities statutes each contain a provision authorizing the Commission to transmit evidence concerning violations of the various

acts to the Attorney General for criminal prosecution.* It must be emphasized that these statutes specifically confer the authority to make a criminal reference only upon the Commission. The language of each of the statutes provides that "[T]he Commission may transmit such evidence ..." (emphasis supplied).** The use of the permissive term "may" gives the Commission the option to make a reference or not; it does not render the form of that reference optional.

*See Securities Act of 1933 (§20(b), 15 U.S.C. §77t(b) (1975); Securities Exchange Act of 1934 §21(e), 15 U.S.C. §78u(e) (1975); Investment Company Act of 1940 §41(e), 15 U.S.C. §80a-41(e) (1964); Investment Advisors Act of 1940 §209(e), 15 U.S.C. §80-b-9(e) (1964); Trust Indenture Act of 1939 §321(a) and (3), 15 U.S.C. §77 uuu(a) and (b) (1964); Public Utility Holding Company Act of 1935 §18(f), 15 U.S.C. §79r(f) (1964).

**The term "Commission" is defined in 15 U.S.C. §78c(15) (and in the appropriate definition sections of each of the other statutes) as "the Securities and Exchange Commission established by section 78d of this title." Section 78d provides that the Securities and Exchange Commission is to be composed of "five commissioners". The regulations promulgated by the SEC adopt the same terminology (see 17 C.F.R. §200.10). Hence, all references in the statutes and regulations to the "Commission" mean exclusively the five appointed Commissioners. The testimony adduced below demonstrates that the SEC employees agree with this (App. 565, 625).

As the Government has pointed out 15 U.S.C. §78d-1(a) grants the Commission the authority to delegate this statutory responsibility to an employee of the Commission. However, that section does itself constitute a delegation of this particular function and it also makes clear that in order for such a delegation to be legally effective it must be done by "published rule or order". The relevant published rules, regulations and orders do not authorize an "informal" criminal reference; indeed, they prohibit it.

The only published regulation cited by the Government in support of the informal procedure is 17 C.F.R. §202.5(b) (Gov't. Br. at 3,n.). That regulation reiterates that the Commission has the authority to make a criminal reference; it says nothing concerning the manner of making the reference or whether that function has been delegated to lower level SEC employees.*

*At the hearing below, the SEC representatives admitted that the Commission itself must authorize the commencement of the first two actions authorized by 17 C.F.R. §202.5(b), i.e., the initiation of administrative proceedings and the initiation of civil injunctive proceedings (App. 625). The Government has not cited one published rule or regulation or offered any sound reason why the third Commission action authorized by §202.5(b), i.e., a criminal reference, is to be treated differently.

That the criminal reference procedure was not intended to be informal is demonstrated by 17 C.F.R. §200.19(b) and 17 C.F.R. §200.21 which prescribe certain procedural requirements for a criminal reference. The former requires review of cases which are the subject of a proposed criminal reference by the Director of the Division of Enforcement (currently Stanley Sporkin)* in collaboration with the SEC's General Counsel. The latter regulation expressly imposes that responsibility on the General Counsel. The language of those regulations clearly do not sanction the informal practice which has recently evolved in this District and which was utilized in this case.

Any doubt that the Commission intended to retain the responsibility for making a criminal reference is dispelled by the published regulations which prohibit any officer or employee of the SEC from disclosing to anyone other than a member, officer

*Mr. Sporkin testified that there presently exists an informal criminal reference procedure. He was, however, unable to cite any statute, rule or regulation which authorized it (App. 548-49).

or employees of the Commission, any information obtained by officers or employees in the course of any examination or investigation under the Act "unless the Commission authorizes the disclosure of such information" 17 C.F.R. §230.122.*

The Government's answer to these clear prohibitions is that an informal criminal reference is authorized by an internal SEC Manual of Administrative Regulations, Section 171 (annexed hereto as Addendum A). While Section 171 was probably intended to set forth the exceptions to the above nondisclosure regulations (see Section 171.01 A.), those exceptions do not apply here. At the outset, Section 171 expressly provides that the authority to make a criminal reference remains with the Commission. This is clear from §171.01 C. which provides that the SEC staff may transmit information to other federal employees "[w]hen the Commission authorizes ... references to the Department of Justice" (emphasis supplied).

*With respect to the Securities Act of 1934, see, 17 C.F.R. §240.0-4p and with respect to the Trust Indenture Act of 1939, see 17 C.F.R. §260.0-6.

Moreover, the Government cannot rely, in this case on Sections 171.06 and 171.07. They are expressly inapplicable to information developed in the course of "formal investigations which have been ordered by the Commission."* In the present case there is no dispute that prior to the SEC's informal criminal reference on December 1, 1976 there was a formal order of investigation executed by the Commission (Tr. 811-12). In view of this fact, only Section 171.08 could apply here, and under that section a Commission

*These two sections obviously are intended to cover the situation where information has been conveyed to the SEC and the SEC determines that it does not warrant further action by the SEC, and, therefore, no formal investigation is ordered by the Commission. In such a circumstance SEC employees are free to transmit the information to the appropriate law enforcement agencies. The Government argued below that the phrase "and other non-public information" found in these sections indicates that the SEC employees were permitted to send the complaint in the TDA case to the United States Attorney. We disagree and in any event more than the mere transmission of a public document was done. The reference was by telephone, and it included a recommendation by the SEC employee that the TDA case be a criminal case (App. 639).

official is authorized only to "recommend to the Commission that information be turned over to such authorities." This section necessarily contemplates that the Commission itself will make the ultimate decision as to whether a criminal reference should be made.

Lastly, the Government's reliance on Section 171 is totally inconsistent with the SEC's own public pronouncements describing its criminal reference procedure. As recently as 1975, in a formal response to a Congressional questionnaire concerning the relationship between the SEC and the Department of

Justice (App. 240-93), the SEC expressly acknowledged that the Commission must approve criminal references after a mandatory review of the criminal reference report by the Director of the Division of Enforcement and the General Counsel (App. 247-49, 251-52, 282-84).^{*} Similarly, an internal SEC manual entitled "Enforcement Manual, Criminal Reference Chapter", which describes the SEC's criminal reference procedure (App. 207-38) also acknowledges the fundamental requirements of approval by the Commission after review by the Office of Criminal Reference, i.e., The Director of the Division of Enforcement and the SEC General Counsel (App. 216-17, 220, 234). This particular manual is also significant because it points out that one of the fundamental purposes of the criminal reference procedure is the protection of the individual's rights. Among the items which must be included in a criminal reference report is a statement as to the status of any pending or contemplated civil action against

^{*}It should be pointed out that the Supreme Court has acknowledged the value of such statements by administrative personnel in ascertaining the nature and purpose of agency procedures. See, e.g., Service v. Dulles, 354 U.S. 363, 377 (1957).

the proposed defendants (App. 233, ¶N). This is included in order to reduce the possibilities of unfairness inherent in parallel civil and criminal proceedings (App. 235-36).^{*} These SEC pronouncements also make clear that the reason why the regulations prescribe approval by the Commission after review by the Director of the Division of Enforcement and the General Counsel is to insure that a proposed criminal reference is "considered by persons of increasing experience and authority" (App. 248-49). Since a criminal reference has such obvious serious effects, only persons of demonstrated wisdom, experience and judgment should make the final determination as to whether the reference should be made.^{**} The correctness of this rationale is borne out by the facts of this case.

^{*}Indeed, Stanley Sporkin testified below that if he had been advised of the proposed reference, which he would have been if the mandated procedure has been followed, he would have advised appellees of it before they executed the consent decree (App. 558). We can never know the answer to the more fundamental question of whether the Commission would have rejected a staff recommendation for a reference in light of the negotiated civil settlement and its consequences.

^{**}As is set forth in the SEC's Annual Reports for 1974 and 1975 (Tr. 709-16), only a relatively small percentage of the matters investigated by the SEC are referred for criminal prosecution. This suggests that the Commission itself and high staff officials have concluded that, as a matter of policy, only certain cases should be referred.

In view of all of the applicable statutes, the SEC's own rules and regulations, and the SEC's own statements on the matter, it is clear that the informal criminal reference procedure utilized by the SEC in this case is unauthorized and indeed prohibited.

B. The SEC Must Abide By
Its Own Regulations

The Supreme Court has repeatedly held that administrative agencies have a duty to observe their own rules and regulations and that breach of that duty necessarily voids the resulting administrative action. Yellin v. United States, 374 U.S. 109 (1973); Vitarelli v. Seaton, 359 U.S. 535 (1959); Service v. Dulles, 354 U.S. 363 (1957).

The leading case on this subject is United States ex rel Accardi v. Shaughnessey, 347 U.S. 260 (1954). There the petitioner who was clearly "deportable", applied to the Immigration and Naturalization Service for suspension of the deportation proceedings pending against him. Pertinent service regulations required review of the petition at various levels within the

*In accord, Smith v. Resor, 406 F.2d 141, 145-46 (2d Cir. 1969); Hammond v. Lenfest, 398 F.2d 705, 715 (2d Cir. 1968); United States v. Coleman, 478 F.2d 1371 (9th Cir. 1973); Electronic Components Corporation of North Carolina v. NLRB, 546 F.2d 1088 (4th Cir. 1976); Note, Violations by Agencies of Their Own Regulations, 87 Harv. L. Rev. 629, 632 (1974).

agency including a final review by the Board of Immigration Appeals, subject to modification by the Attorney General. The Appeals Board was charged by the regulations to "exercise discretion" in the disposition of such cases. The Attorney General in Accardi released, prior to the Board's consideration of petitioner's case, a list of persons he wanted deported. Since petitioner was on that list, the Board for all intents and purposes failed to exercise its independent judgment. The Court in ordering the Appeals Board to reconsider the matter and to use its own discretion in disposing of the petition observed (347 U.S. at 266-68):

"The clear import of broad provisions for a final review by the Attorney General himself would be meaningless if the Board were not expected to render a decision in accord with its own collective belief And if the word 'discretion' means anything as a statutory or administrative grant of power, it means that the recipient must exercise his authority according to his own understanding and conscience."
(emphasis added)

* * *

"In short, as long as the regulations remain operative, the Attorney General denies himself the right to sidestep the Board to dictate its decision in any manner.

* * *

"... we object to the Board's alleged
failure to exercise its own discretion
contrary to existing regulations."
(emphasis in original)

In accord, Yellin v. United States, supra.

The present case is even more egregious than Accardi since it involves a wholesale abdication by the Commission of its decision making responsibility with respect to a criminal reference in favor of individuals at lower echelons within the agency. Moreover, it is impossible to rectify the SEC's breach of its own regulations by requiring the Commissioners to consider now whether a reference should be made since the Government has, as a direct result of that reference, already procured an indictment. The only conceivable remedy here is dismissal of the indictment.

The SEC's noncompliance with its own rules and regulations may not be excused on the ground that the Commission's decision whether to make a criminal reference is a matter solely within its discretion. United States v. Heffner, 420 F.2d 809, 812 (4th Cir. 1969); Service v. Dulles, supra; Vitarelli v. Seaton, supra; Hammond v. Lenfest, supra.*

*While the SEC could have changed its regulations to adopt an informal criminal reference procedure, as noted above, it could only do so "by published rule and order" (con't)

When it is demonstrated that an agency has not followed its rules and regulations, courts have not hesitated to undo the results of the illegal administrative action. (See cases cited supra at 20) The Court in Pacific Molasses Company v. F.T.C., 356 F.2d 386, 390 (5th Cir. 1966) stated the rule succinctly as follows:

"If any agency in its proceedings violates its rules and prejudice results, any action taken as a result of the proceedings cannot stand."

The prejudice in this case is the indictment itself which is the direct and necessary result of the invalid

* (footnote con't)

15 U.S.C. §78d-1(a). It may not effectively repeal existing rules and regulations by an unannounced internal decision to ignore them in the future. In Briscoe v. Kusper, 435 F.2d 1046 (7th Cir. 1970), the Court invalidated a similar unannounced deviation by an administrative agency from its established procedure, stating (id. at 1055):

"The Board may not deviate from such prior rules of decision on the applicability of a fundamental directive without announcing in advance its change in policy Until such time as the Board makes public its new determination, it is constitutionally prohibited from imposing that rule on unsuspecting persons." (emphasis supplied).

See also 5 U.S.C. §553 which specifies the required procedures for agency rule-making. It should also be pointed out that there is no testimony here that the SEC has totally abandoned the formal criminal reference procedure. In essence the testimony is rather that on a purely ad hoc basis regional staff personnel decide themselves whether or not to follow the informal or formal procedure.

criminal reference. It is no answer that the Grand Jury is a supervening cause of the indictment because, if the SEC's rules had been followed here, the Commission may have decided not to make the reference. In that event this particular indictment would not have been returned. Moreover, the possibility that the Commissioners might have made a criminal reference, had they been given the opportunity to consider the matter, is beside the point; the plain fact is they never exercised that judgment and under Accardi they were required to do so. As the Court in United States v. Heffner, 420 F.2d 809, 813 (4th Cir. 1969):

"The Accardi doctrine furthermore requires a reversal irrespective of whether a new trial will produce that same verdict."

See also Yellin v. United States, supra, 374 U.S. at 121.

Significantly, the Accardi doctrine is not limited to cases in which the agency itself imposes a sanction. It applies equally to agency action leading up to the institution of charges in another forum. In United States v. Jones, 368 F.2d 795 (2d Cir. 1966), United States Treasury officials failed

to follow Treasury regulations which required them to notify the defendant of his duty to register upon re-entry to the country. This Court reversed his conviction for failing to register on the same narrow grounds we rely upon here. The Court stated (id. at 799):

"Our decision rests on the principle that because the Government has failed to follow its own regulation, promulgated in the proper exercise of the Secretary of the Treasury's discretion, its action can have no effect. In other words, having failed to supply Jones with Form 3231 and to give him the opportunity to register provided for in the Regulation, his arrest and indictment are invalid. There is no novelty in holding that where an official is given discretionary power by statute, promulgates regulations as to how the power is to be exercised and then fails to follow his own regulations, the action is of no effect." (emphasis added).

It is important to stress that the Court's reversal of the conviction was based solely on the Court's determination that the Treasury Regulation had not been followed. The only remedy considered by the Court was dismissal of the indictment which followed.

In United States v. Leahy, 434 F.2d 7 (1st Cir. 1970), the Court affirmed the exclusion of evidence from a criminal trial because employees of an administrative agency had obtained the evidence in contravention of certain agency rules. Even though the United States Attorney was in no way involved in the violation of the agency rule, the Court held it necessary to,

"exclude this evidence so that agencies' will be compelled to adhere to the standards of behavior that they have formally and purposely adopted in the light of the requirements of the Constitution, even though these standards may go somewhat further than the Constitution requires."
434 F.2d at 10.*

That same remedy -- the denial to the prosecutor of the fruits of the illegal administrative action -- should be applied here to invalidate the indictment.

*The present case is not distinguishable from United States v. Jones, 368 F.2d 795 (2d Cir. 1966) and United States v. Leahy, 434 F.2d 7 (1st Cir. 1970) on the ground that the regulations in those cases had for their purpose the protection of individual rights. That is also the purpose of the regulations at issue here. See discussion in Point A above. Moreover, this case also involves the application of the Accardi doctrine to an administrative agency's failure or refusal to exercise the discretion required by the law.

Recission of the consent judgment would clearly not remedy the SEC's failure to comply with its rules and regulations. As the Government has argued, the remedy should fit the wrong. For example, if the Commission had ignored the regulation which requires Commission approval of a settlement, then perhaps recission of that settlement would be the appropriate remedy. Here, however, the invalid administrative action was the making of a criminal reference without Commission approval and without prior consultation with the Director of the Division of Enforcement and the General Counsel and that occurred prior to the execution by all of the final settlement. Under the present circumstances, vitiating the criminal reference itself is a meaningless gesture, if the consequence of that reference -- the indictment -- is permitted to stand.

In response to this argument below, the Government relied on United States v. Leonard, 524 F.2d 1076, 1086 (2d Cir. 1975), cert. denied, 425 U.S. 958 where the issue was whether the failure of the Internal Revenue Service to follow an internal instruction

with respect to Miranda warnings required suppression of evidence. Leonard is distinguishable from the present case on many grounds, but principally because the regulations here are not merely informal internal directives or suggestions as they were in Leonard but are published mandatory statutes and regulations which the SEC is obligated to follow.*

Closer to the mark than Leonard and National Student Marketing is United States v. Giordano, 416 U.S. 505 (1947), affirming 469 F.2d 522 (4th Cir. 1972), where the Supreme Court sustained a lower court decision to suppress wiretap evidence because the Government failed to comply with a statute which required the

*This case is also distinguishable from Securities and Exchange Commission v. National Student Marketing, 538 F.2d 404 (D.C. Cir. 1976), cert. denied U.S. which the District Court cited below (App. 69). Unlike appellees who have demonstrated a pervasive regulatory scheme affirmatively establishing the procedures appellees seek to enforce, documented not only in published regulations and internal memoranda, but in public pronouncements by the SEC, the defendants in National Student Marketing relied on a single, ambiguous, internal, non-public memorandum as the exclusive basis of their claim. The Court concluded that "had the Commission intended to establish a procedural rule which, if breached, would require dismissal of a complaint, we think it would have said so in language far clearer and more direct." 538 F.2d at 407. Here the Commission has done precisely that.

United States Attorney General to authorize personally an application for the wire tap. In construing statutory language analogous to the statutes and regulations involved here, the Supreme Court held (416 U.S. at 515-16):

"The Act plainly calls for the prior, informed judgment of enforcement officers desiring court approval for intercept authority, and investigative personnel may not themselves ask a judge for authority to wiretap or eavesdrop. The mature judgment of a particular, responsible Department of Justice official is interposed as a critical precondition to any judicial order."

Many of the arguments advanced by the Government in Giordano are similar to those asserted by the Government in this case. For example, the Government in Giordano argued that the failure to obtain approval by the Attorney General, relying instead on an individual designated by him, was a mere technicality. The Fourth Circuit rejected this attempt to trivialize a clear breach of the statutory requirements, stating (469 F.2d at 530):

"We cannot relegate provision after provision to oblivion by terming each a mere 'technicality' -- or else we leave the statute a shadow of itself, an apparition without substance."

So here it would totally emasculate the statutes and SEC rules and regulations cited above to allow the judgment of lower echelon SEC employees to be substituted for that of the Commission in determining whether a case should be referred for criminal prosecution.

The Fourth Circuit also quickly disposed of another argument advanced by the Government in Giordano which is similar to the Government's argument here that appellees suffered no prejudice as a result of the SEC's breach of its regulations. The Court stated (469 F.2d at 530-31):

"As a last resort, the Government submits that even if the authorization procedures used were deficient and the application and subsequent wiretap order irregular and misleading in some respects, 'there is no reason to apply the drastic remedy of suppression to correct a technical defect in procedure.' This is a beautiful example of the bootstrap technique. First the Government minimizes the violation of the various statutory provisions involved, characterizing them as 'technical defects,' and then in typical bootstrap fashion postulates that for minor violations there should be no sanctions

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"It is appropriate here to recall Justice Brandeis' famous admonition given nearly forty-five years ago in *Olmstead v. United States*, 277 U.S. 438, 385, 48 S.Ct. 564, 575, 72 L.Ed. 944 (1929) (dissenting), that when 'government becomes a lawbreaker, it breeds contempt for law.' Similarly, when government consistently tramples upon those parts of the law that do not suit its momentary purpose and seeks to justify its conduct by sophistic argumentation, neither respect for the law nor societal order is promoted...."

We respectfully submit that the principal issues raised by this appeal are whether the Government must be honorable and even-handed in its dealings with citizens and whether the Government is obliged to obey its own statutes and regulations. If the answer to these questions is to be in the affirmative the indictment must be dismissed.

POINT II

THE UNITED STATES ATTORNEY'S PARTICIPATION
IN THE INFORMAL CRIMINAL REFERENCE RENDERS
HIM ACCOUNTABLE FOR THE MISCONDUCT OF
THE SEC EMPLOYEES

In October, 1975, SEC staff attorney Perlmutter, after a discussion with Tucker, telephoned their friend and former associate Assistant United States Attorney Sorkin (Tr. 1329-38), to tell him they had a great case for criminal prosecution. From that point and continuing up through December 1, 1975, when the "formal-informal" reference was made from Tucker to Wing (*infra*, 7-8) there were numerous further discussions about making a criminal case in TDA, all concealed from the defendants and their counsel (App. 642-48, Tr. 1463-64). Later, the Government presented the case to the grand jury using much of the information it had gathered from the SEC. Having willfully participated in this informal criminal reference scheme and having knowingly accepted the fruits of it, the United States Attorney is bound by the actions of his acquired agents. We submit he cannot disavow their prior misconduct performed

in the carrying out of a procedure which was devised by and adopted for the benefit of the Government (Tr. 718-19, 1299-1303).*

The Government should not now have it both ways. Either statutory authority exists which makes the SEC an independent fact gathering agency which then formally refers cases after approval by the Commission (see Point I, infra), or the SEC staff attorneys are acting as agents for the United States Attorney in gathering evidence for indictment and conviction, as well as for civil settlement and disgorgement. If the United States Attorney chooses to ignore the applicable published rules and regulations and to promote and foster the informal relationship (Tr. 1299-1303), he must bear the responsibility for the ignoble actions of his agents.

In short, if the United States Attorney encourages this unpublished, non-statutory procedure, he should be prepared to accept the full responsibility for the conduct of the people involved in the implementation of such a device. As Judge Haight put it (App. 82):

*Under these circumstances the cases cited by the Government (Gov't. Br. 29) are inapposite. They virtually all involve the failure of the prosecution to turn over to the defendants information required under Brady v. Maryland, 373 U.S. 83 (1973). Moreover, in those cases there was no suggestion that the prosecution was aware that the requested information was available to the agency or that there existed the type of unauthorized relationship which both agencies here have adopted for their mutual benefit.

"[i]t is Government, in all offices and functions, which must be held to standards of fair and honest dealing with the citizens of the Republic."

Conclusion

For the foregoing reasons the District Court's dismissal of the indictment should be affirmed.

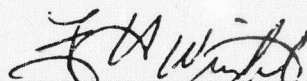
Dated: October 21, 1977

Respectfully submitted,

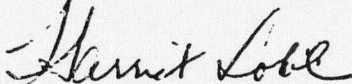
GRAND & OSTROW
Attorneys for Defendant-
Appellee Alan E. Sandberg
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New York, N.Y. 10022

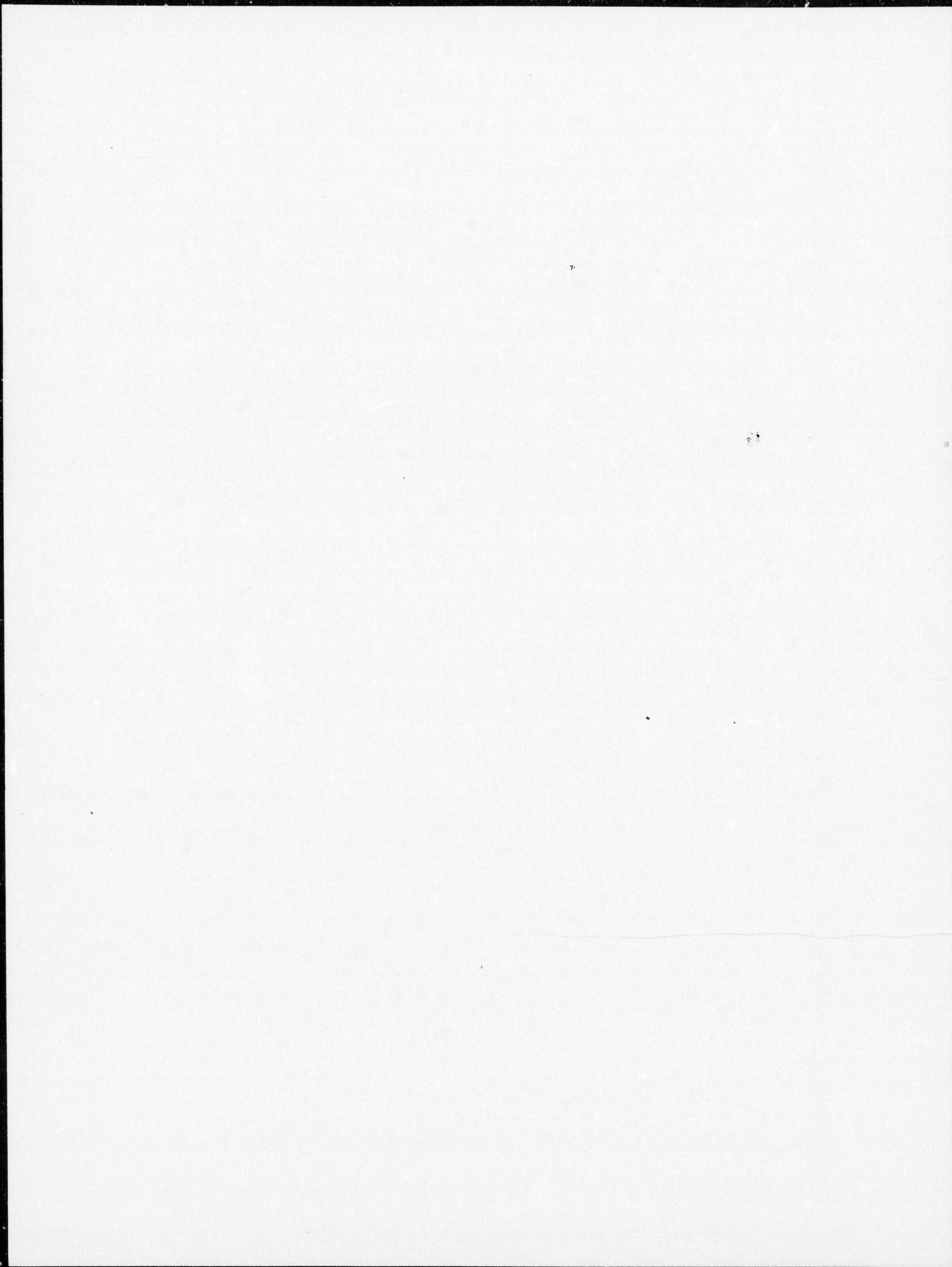
CERTIFICATE OF SERVICE

I hereby certify that true and correct copies of the foregoing Brief have been served by hand on David A. Cutner, Esq., Assistant United States Attorney, One St. Andrew's Plaza, New York, N.Y., attorney for appellant; and by mail on Bender & Frankel, Esqs., 225 Broadway, New York, N.Y. 10007, attorneys for defendants-appellees Douglas P. Fields and Frederick M. Friedman; Orans, Elsen & Polstein, Esqs., One Rockefeller Plaza, New York, N.Y. 10020, attorneys for defendant-appellee, Peter S. Davis; and Howard Wilson, Esq., c/o Hochman, Salkin and DeRoy, 9100 Wilshire Blvd., Los Angeles, California 90212, attorney for defendant-appellee Eric Berge, all of the 21st day of October, 1977.


Frank H. Wright

Sworn to before me this
21st day of October, 1977





ADDENDUM "A"



1:171.01

9/24/74

Section 171: COOPERATION WITH FEDERAL, STATE AND FOREIGN GOVERNMENT
AUTHORITIES AND WITH SELF-REGULATORY ORGANIZATIONS

- 171.01 Purpose and Policy. This Section states Commission policy on making available to Federal, State and Foreign government authorities and national securities exchanges and national securities associations information developed in the course of investigations and other non-public information, and delegates discretionary authority to make such information available in situations covered by this section. This Section is intended to facilitate cooperation with other enforcement agencies and to relieve Regional Administrators and Directors of Divisions and members of their staffs of the requirement to obtain prior authority from the Commission when it is obviously in the public interest to supply such information.
- A. Attention is directed to the Commission's rules under the acts it administers prohibiting disclosure by officers and employees of information or documents obtained in the course of any examination or investigation or any other non-public records of the Commission, unless the Commission authorizes the disclosure of such information or documents as not being contrary to the public interest. This Section constitutes such authorization by the Commission in cases which fall within its terms. Cases where subpoenas are served upon Commission personnel are not within the scope of this Section and will continue to be handled in accordance with the above rules.
 - B. The prohibition against use of non-public information or documents without specific authorization by the Commission does not apply to the use of such materials as necessary or appropriate by members of its staff in pursuing Commission investigations. Thus, for example, documents obtained from a witness may be used in the examination of other witnesses or submitted for document analysis. Similarly, testimony of a witness may be used in examining other witnesses. In short, such information may be used as is necessary to facilitate the development of Commission matters.
 - C. When the Commission authorizes the institution of actions, or reference to the Department of Justice, the staff also is authorized to use such non-public material as may be required for the effective presentation or prosecution of the case. When requests for non-public material are made by respondents or defendants, and the staff is in doubt as to the propriety of disclosing such material in the course of such litigation, it may present such matters to the Commission for appropriate advice or authorization.

1:171.02

9/24/74

Section 171: COOPERATION WITH FEDERAL, STATE AND FOREIGN GOVERNMENT
AUTHORITIES AND WITH SELF-REGULATORY ORGANIZATIONS

171.02 Responsibility and Redelelegation.

- A. Authority to act in matters covered in this Section is hereby delegated by the Commission to Directors of Divisions and Regional Administrators having cognizance over cases in which cooperation with other Federal, State or foreign authorities or self-regulatory organizations is in the public interest. These Commission officials may redelegate authority to act to designated members of their staffs.
- B. When the term Commission officials is used hereafter in this section, it means the officers enumerated in the preceding paragraph.

171.03 Authority.

Rule 122, Securities Act of 1933
Rule 0-4, Securities Exchange Act of 1934
Rule 104(c), Public Utility Holding Company Act of 1935
Rule 0-6, Trust Indenture Act of 1939
Rule 26(c), Commission's Rules of Practice
Commission Minute of September 30, 1957, adopting policy memorandum of August 28, 1957.

- 171.04 Confidential Nature of Information. If public disclosure of information being given to another Federal, a State or foreign government authority or self-regulatory organization may interfere with Commission enforcement activities, the Commission official involved will inform the receiving agency or organization that the information is supplied with the understanding that it will be held confidential and not disclosed to the public without authorization by the Commission.

- 171.05 State Agencies. Referral of information to State agencies for enforcement under State law is governed by the following instructions:

- A. Commission officials are authorized in their discretion to make available to appropriate State authorities all material developed in pending investigations and other non-public information, other than formal investigations specifically ordered by the Commission, with a view to enforcement action by such State authorities, if the Commission official determines:

- (1) The investigation appears to disclose a violation of State law; and

1:171.05A(2)

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AUTHORITIES AND WITH SELF-REGULATORY ORGANIZATIONS

- 171.05 (2) The Commission official is of the opinion that the case can better be dealt with by State authorities than by the Commission primarily when there would be substantial difficulty moving a case under Federal law or if the case is primarily of local interest; and
- (3) The Commission official has reason to believe that the State authorities will proceed promptly with investigation and will enforce any State law found to have been violated.
- B. The primary purpose of this procedure is to conserve time and manpower. This procedure normally will not be employed where the Commission will have to continue the investigation because the State authorities are not equipped to perform this function.

171.06 Cooperation With Other Federal Law Enforcement Authorities. Since Commission cases frequently involve violations of the mail fraud statute and may involve other Federal statutes, the Commission recommends and encourages full cooperation with inspectors of the United States Post Office Department and other Federal law enforcement officials. Commission officials are authorized in their discretion to make information developed in the course of their investigations, other than formal investigations which have been ordered by the Commission, and other non-public information available to these officials and to render such investigative assistance as may be required.

171.07 Furnishing Information to Other State and Federal Law Enforcement Agencies. In cases not falling within Subsections .05 and .06 of this Section, that is, situations other than referral of a matter for State enforcement action, or cooperation with the Post Office Department or other Federal law enforcement officials, Commission officials are authorized in their discretion to make available to Federal and State law enforcement to Federal and State law enforcement agencies information developed in the course of an investigation other than a formal investigation which has been ordered by the Commission and other non-public information when the Commission official is satisfied that such action clearly will not interfere with the Commission's enforcement functions in the particular case or in other cases.

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- 171.08 Disclosure of Information in Formal Investigations. If a Commission official believes that a formal investigation which has been ordered by the Commission should be referred to Federal or State authorities for enforcement action under the foregoing standards, the Commission official may recommend to the Commission that information be turned over to such authorities.
- 171.09 Foreign Government Authorities. Cooperation with foreign government authorities is governed by the following instructions:
- A. Commission officials are authorized, in their discretion, to make available to foreign government authorities information developed in the course of an investigation and other non-public information when the Commission official believes that such action will not interfere with the Commission's enforcement functions. The importance of cooperating with foreign government authorities should be emphasized. If it is necessary to undertake any investigative work in order to supply information requested by a foreign government authority, Commission officials are authorized in their discretion to have such work performed by the Commission staff.
 - B. In order for the Commission to maintain proper control over its relations with foreign government authorities and to permit proper liaison with the Department of State, Commission officials should obtain prior authorization from the Division of Enforcement before:
 - (1) Requesting a foreign government authority to supply information, other than information which may be supplied without difficulty or burden upon foreign government authorities.
 - (2) Sending Commission personnel to a foreign country on official business.
- 171.10 Furnishing Information to National Securities Exchanges, National Securities Associations, and Foreign Stock Exchanges or Other Foreign Self-Regulatory Organizations. Subject to the restrictions in subsection .04 above, Commission officials are authorized, when in their discretion it is in the public interest, to make available to any national securities exchange or national securities association, or foreign stock exchange or other foreign self-regulatory organization, such non-public information, documents or records, or any part thereof, as are necessary or appropriate to the conduct of the self-regulatory activities of such exchange or association.

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AUTHORITIES AND WITH SELF-REGULATORY ORGANIZATIONS

171.11 Documentation and Procedures. The following will be observed in all actions under this Section:

- A. When oral information is supplied pursuant to this Section, a record will be prepared and kept in the case correspondence file if opened, or otherwise in the general correspondence file, to indicate the nature of the information furnished.
- B. When non-public documents or files are to be examined on Commission premises, the authorizing Commission official will prepare a similar record to indicate the documents and files made available, and make arrangements for the examination.
- C. Official files and unbound original documents may be loaned only to Federal agencies. Copies may be loaned or given to Federal, State or foreign agencies or to self-regulatory organizations pursuant to this Section. Before releasing the material, the Commission official:
 - (1) Will prepare in duplicate a reasonably detailed receipt giving specific identification of the official files (i.e., the complete file number, name, and copy designation as shown on the file cover), or an accurate description of the document.
 - (2) Will send one copy of such receipt immediately to the Office of Records (if in the headquarters offices) or to the Administrative Clerk or equivalent (if in a regional office).
 - (3) Will send or deliver the original of the receipt with the material. After the receipt has been signed by the responsible official of the receiving authority or organization and returned, it will be placed in the case correspondence file if a case file has been opened, otherwise in the general correspondence file.
 - (4) May arrange for delivery himself or through the Office of Records or the Administrative Clerk or equivalent.
 - (5) Will make and follow-up arrangements for the return to the Commission of any official files and original unbound documents loaned.

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Section 171: COOPERATION WITH FEDERAL, STATE AND FOREIGN GOVERNMENT
AUTHORITIES AND WITH SELF-REGULATORY ORGANIZATIONS

- 171.11 D. If the authority delegated in this Section does not apply, the release of the information or document must be specifically authorized by the Commission. After receiving such authorization, the Commission official will follow the appropriate procedures outlined above.
- E. When appropriate, information copies of the records and receipts referred to in paragraphs A, B and C above will be furnished to other Divisions and Offices having an interest in specific cases.
- 171.12 Consultations for Advice. If a Regional Administrator is uncertain as to the desirability of supplying information in compliance with a request or otherwise, he may communicate the request to the headquarters division having primary interest in the investigation, with a statement of the reasons for and against making the information available, and request instructions. If such a request originated in the Department of Justice or the Federal Bureau of Investigation, the Regional Administrator will communicate with the General Counsel and send a copy to the appropriate division.
- 171.13 Reporting Delegations of Authority. In the headquarters offices, each redelegation of the authority to act under this Section must be reported, in writing, to the Records Officer prior to any exercise of the redelegation. In the regional offices, redelegations must be reported to the Administrative Clerk.
- 171.14 Superseded Instructions. This Section supersedes all prior material issued upon this subject, and any other existing instructions in conflict with the provisions of this Section.

ADDENDUM "B"



15 U.S.C. §77t Injunctions and prosecution of offenses

(b) Whenever it shall appear to the Commission that any person is engaged or about to engage in any acts or practices which constitute or will constitute a violation of the provisions of this subchapter, or of any rule or regulation prescribed under authority thereof, it may in its discretion, bring an action in any district court of the United States or United States court of any Territory, to enjoin such acts or practices, and upon a proper showing a permanent or temporary injunction or restraining order shall be granted without bond. The Commission may transmit such evidence as may be available concerning such acts or practices to the Attorney General who may, in his discretion, institute the necessary criminal proceedings under this subchapter.

15 U.S.C. §78u Investigations; injunctions and prosecution of offenses

(e) Whenever it shall appear to the Commission that any person is engaged or about to engage in any acts or practices which constitute or will constitute a violation of the provisions of this chapter, or of any rule or regulation thereunder, it may in its discretion bring an action in the proper district court of the United States or the United States courts of any Territory or other place subject to the jurisdiction of the United States, to enjoin such acts or practices, and upon a proper showing a permanent or temporary injunction or restraining order shall be granted without bond. The Commission may transmit such evidence as may be available concerning such acts or practices to the Attorney General, who may, in his discretion, institute the necessary criminal proceedings under this chapter.

15 U.S.C. §78c Definitions and application - Definitions

(15) The term "Commission" means the Securities and Exchange Commission established by section 78d of this title.

17 C.F.R. §200.10 The Commission.

The Commission is composed of five members, The Commission is assisted by a staff, which includes lawyers, accountants, engineers, financial security analysts, investigators and examiners, as well as administrative and clerical employees.

15 U.S.C. §78d-1 Delegation of functions by Commission - Authorization; functions delegable; eligible persons; application of other laws

(a) In addition to its existing authority, the Securities and Exchange Commission, hereinafter referred to as the "Commission", shall have the authority to delegate, by published order or rule, any of its functions to a division of the Commission, an individual Commissioner, a hearing examiner, or an employee or employee board, including functions with respect to hearing, determining, ordering, certifying, reporting, or otherwise acting as to any work, business, or matter:

17 C.F.R. §202.5 Enforcement activities.

(b) Where it appears after investigation or otherwise that there has been a violation of any of the provisions of the acts administered by the Commission or the rules or regulations thereunder, the Commission may take one or more of the following actions: institution of administrative proceedings looking to the imposition of remedial sanctions, initiation of injunction proceedings in the courts, and, in the

case of a willful violation, reference of the matter to the Department of Justice for criminal prosecution. The Commission may also on some occasions refer the matter to other Federal agencies, State authorities or organizations such as the stock exchanges or the National Association of Securities Dealers, Inc.

17 C.F.R. §200.19b Director of the Division of Enforcement.

The Director of the Division of Enforcement is responsible to the Commission for the supervision and conduct of all of the enforcement activities under each of the acts administered by the Commission and the investigations relating thereto. The Director is responsible also for the institution of administrative and injunctive actions arising out of such investigations and enforcement activities and for the determination of whether the available evidence supports the allegations in the proposed complaint. In addition, the Director is responsible, in collaboration with the General Counsel, for the review of cases to be referred to the Department of Justice with a recommendation for criminal prosecution.

17 C.F.R. §200.21 The General Counsel.

The General Counsel is the chief legal officer of the Commission and is responsible for the representation of the Commission in judicial proceedings in which it is involved as a party or as amicus curiae, directing and supervising all civil litigation in the U.S. District Courts (except District Court proceedings under Chapter X of the Bankruptcy Act), and representing the Commission in all cases in appellate courts. He is responsible, in collaboration with the Division of Enforcement, for review of cases to be referred to the Department of Justice with a recommendation for criminal prosecution.

17 C.F.R. §230.122 Nondisclosure of information obtained
in the court of examinations and
investigations.

Information or documents obtained by officers or employees of the Commission in the course of any examination or investigation pursuant to section 8(e) or 20(a) (48 Stat. 80, 86; 15 U.S.C. 77h(e), 77t(a)) shall, unless made a matter of public record, be deemed confidential. Officers and employees are hereby prohibited from making such confidential information or documents or any other non-public records of the Commission available to anyone other than a member, officer, or employee of the Commission, unless the Commission authorizes the disclosure of such information or the production of such documents as not being contrary to the public interest. Any officer or employee who is served with a subpoena requiring the disclosure of such information or the production of such documents shall appear in court and, unless the authorization described in the preceding sentence shall have been given, shall respectfully decline to disclose the information or produce the documents called for, basing his refusal upon this section. Any officer or employee who is served with such a subpoena shall promptly advise the Commission of the service of such subpoena, the nature of the information or documents sought, and any circumstances which may bear upon the desirability of making available such information or documents.

